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SENSITIVE

STATE FOR SCA/INS AND EEB/IFD/OMA
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TAGS: ECON EFIN EAID MV
SUBJECT: MALDIVES: ECONOMY GREW BY 5.7% IN 2008; DOWNTURN EXPECTED IN 2009

Ref: (a) COLOMBO 273
b) 08 COLOMBO 1075

¶1. (U) Summary: In 2008, the Maldivian economy grew by 5.7%, down from 7.2% growth in 2007. Tourism and fisheries, the mainstays of the economy, fared poorly. Tourism grew by only 2.9% compared to 9.4% in 2007. The fisheries sector contracted for the second straight year. While these key sectors underperformed, construction, government administration, transport, communication, electricity, water and financial services contributed to growth. Due to high dependence on tourism, the Maldivian economy is deeply vulnerable to the global recession. ADB forecasts growth to slow sharply to 1.1% in 2009. End Summary.

GDP UP BY 5.7%

¶2. (U) According to the Maldives Monetary Authority (MMA), Maldives' economy grew by 5.7% in 2008 - lower than its pre-tsunami average annual growth rate of 7.4%. Growth was also slower than the 7.2% experienced in 2007. GDP totaled around $1.2 billion, or about $3,900 per capita. Maldives continues to have the highest per-capita GDP in South Asia, far exceeding the average of around $1,000 in the region. Inflation increased sharply to 12.3% in 2008 from 7.4% in 2007 as import prices for oil, food and construction materials increased. Government expenditure also increased sharply. Monetary growth remained high at more than 20% in 2007 and 2008. Domestic credit to both government and private sector expanded sharply during this period.

TOURISM GROWTH DOWN, FISHERIES HURTING, OTHER SECTORS MANAGING

¶3. (U) Tourism, the most important economic sector and directly accounting for 27% of GDP, grew by just 2.9% compared with 9.4% growth in 2007. Arrivals rose by only 1% to 683,000. Overall tourism income in 2008 was estimated at around $644 million. Europe remains the largest market for Maldives (primarily UK and Italy), accounting for more than 70% of visitors; however, arrivals from Europe were flat in 2008. China and Japan together account for another 11%. Tourism-related industries, such as transport and communications, grew by 7.5%. Construction, which accounts for 6.4% of GDP, grew by 13%. Government administration, accounting for a significant 17% of GDP, also grew by 13%. Manufacturing accounts for about 7% of GDP; it grew by about 2%.

¶4. (U) Fisheries, which accounts for only 4.2% of GDP but is important in terms of employment and exports, recorded a 2.7% decline in 2008. Fish exports, the largest export product of Maldives, increased by 17% due to higher prices. This was despite a sharp decline in the fish catch in the past two years, the reasons for which are not clear.

TRADE DEFICIT UP

¶5. (U) On the external side, the trade deficit increased significantly by 21% to $890 million. The oil bill rose considerably by 55%. The food import bill also increased sharply by 21% to $212 million. Tourism earnings of about $700 million helped to partly offset the large trade deficit. Maldives recorded a current account deficit of $590 million in 2008 (47% of GDP). Although the financial account recorded large inflows, the balance of payments recorded a deficit of $68 million. At year end, gross external reserves stood at $241 million, sufficient to cover 2.1 months of imports. Total outstanding external debt stock stood at $471 million. An Indian government loan of $100 million in late 2008 helped to increase reserves.

¶6. (U) According to the ADB, Maldives' GDP growth is expected to slow sharply to a mere 1.1% in 2009 and gradually recover to 1.5% in ¶2010. ADB says projections depend on the new government's ability to introduce meaningful reforms and on the tourism sector's performance. The latest statistics show a sharp 15% drop in tourist arrivals in February following a 5% decline (year-on-year) in January arrivals. Tourists from Maldives' two biggest markets, Italy and UK, have seen drastic drops. President Nasheed travelled

to Italy in February 2009 in an effort to promote tourism; he will also meet UK tour operators during an official visit to the UK beginning April 6. However, according to tourist industry sources, bookings for the low season (May-September) are half the usual. Resorts are offering special packages to minimize losses and are trying to diversify into markets, including India.

The Road Ahead

¶7. (SBU) The government is forecasting a substantial drop in revenue in 2009 due to a decline in tourist arrivals and a decrease in revenue from import taxes. Maldives was already facing a large budget deficit of 32% of GDP in 2009 according to estimates prepared by the previous government and passed by the present government (ref b). Therefore unless expenditures are rationalized significantly, the deficit will increase further (according to some estimates to 50% of GDP) due to these losses. President Nasheed has promised to revise the budget in early 2009. Post will report on the Maldives government fiscal outturn for 2008 and latest budget forecasts for 2009 when the government releases its revised budget in the coming weeks.